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UNCLAS SANTO DOMINGO 003129

SIPDIS

SENSITIVE
SIPDIS

DEPT FOR WHA/CAR, EB/TPP/ABT THOMAS LERSTEN;
COMMERCE FOR ITA/OTEXA MARIA D'ANDREA,
4322/ITA/MAC/WH/CARIBBEAN BASIN DIVISION;
3134/ITA/USFCS/RD/WH;
DEPT AND WHITE HOUSE PASS TO USTR ABIOLA HEYLIGER

E.O. 12958: N/A
TAGS: ECON ETRD KTEX DR
SUBJECT: DOMINICAN TEXTILES AND APPAREL - STATS AND
PROJECTED COMPETITIVENESS

REF: STATE 12958

¶1. (U) Summary. Textile and apparel production represents an important part of the Dominican Republic's economy. Half of all companies in the Dominican Free Trade Zones (FTZs) are textile and apparel related companies and 98 percent of all Dominican textile and apparel companies are located in the FTZs. The Dominican Republic is one of the largest consumers of U.S. textile inputs in Central America and the Caribbean region. The January 1, 2005 phase-out of textile and apparel quotas, the overvalued peso, the unstable electricity situation, and recent increases in customs processing charges have diminished the profitability of the sector. The Central American and Dominican Republic Free Trade Agreement (CAFTA-DR) should improve the situation, once it enters into force, probably by early 2007, but it is only the first step to secure revitalization of the sector. End Summary.

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FACTS AND FIGURES FOR 2005
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-Total value of industrial production in the Dominican Republic: USD 4.365 billion.
-Total textile and apparel production value: USD 1.904 billion (a decline of 10 percent from 2004)
-Textile/apparel's share of total FTZ exports: 40 percent
-Textile/apparel's share of total exports: 31 percent
-Textile/apparel's share of total FTZ imports: 45 percent
-Textile/apparel's share of total imports for domestic use: less than one percent
-Total manufacturing employment in the FTZs: 152,955 (a decline of 18 percent from 2004)
-Total textile and apparel employment: 91,491 (a decline of 30 percent from 2004)

(Sources: the Central Bank, the Dominican Association of Free Trade Zones (ADOZONA), and the National Council for Free Trade Zone Exportation (CNZFE)).

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REACTION TO THE PHASE-OUT OF QUOTAS
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¶2. (U) After the expiration of the quotas of the Multi-Fibre Accord, there was an evident drop in the average price of most goods exported from the Dominican Republic to the United States in 2005. However, in the first semester of 2006,

prices have risen, mainly due to increases in energy prices and a mandatory salary increase.

¶3. (U) The phase-out of quotas also affected the level of textile production in the Dominican Republic. A recent survey by the National Council of Free Trade Zones reveals that the level of production, which is directly proportional to the number of orders, was less in 2005 than in 2004. Accordingly, a total of 98 textile and apparel companies have closed down either temporarily or permanently, including both local and foreign companies.

¶4. (U) The safeguard measures set by the United States on China on more than 10 textile categories have had a slight positive short term impact on Dominican textile exports. However, these measures are only temporary. The European Union's restrictions on certain exports of textiles and apparel from China have not affected Dominican export prospects because 95 percent of Dominican textile exports go to the United States.

¶5. (U) Although the phase-out of quotas has negatively affected the Dominican Republic, the current administration has not considered imposing any safeguards or other measures to counter imports of Chinese textile and apparel products into the Dominican Republic.

¶6. (U) In an attempt to compete with Chinese textiles, the Dominican Association of Free Trade Zones requested the Minister of Labor to modify Resolution No. 6/2004 in order to delay the second part of a salary increase which was to have taken place on April 4, 2005. This request was granted via Resolution No. 2/2005, which postponed the salary increase to January 2, 2006.

¶7. (U) ADOZONA and CNZFE are working together with the textile manufacturers to offset the challenges they face with the phase-out of quotas. They continue to take advantage of their close proximity to the United States by providing services that expedite the supply chain. For example, some companies package and tag finished products, such as Hanes wear, so that the products can be shipped from the Dominican Republic directly to the stores. A small number of firms are engaged relatively high tech custom cutting and sewing.

¶8. (U) The Dominican economy benefits from improvements in port facilities. The privately owned multimodal port of Caucedo, which opened in December, 2004, recently received its certification under the Container Security Initiative (CSI) administered by the Department of Homeland Security. With CSI, textile and apparel producers will be able to ship their products to the United State as "pre-cleared," which decreases shipment time and costs.

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CAFTA-DR
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¶9. (U) The implementation of regional trade agreement CAFTA-DR will provide the textile/apparel sector in the Dominican Republic permanent duty-free access to the U.S. market, unlimited duty-free use of local and regional fabric and yarns, limited access to woven-fabrics constructed in NAFTA countries, unlimited use of extra-regional trims and buttons, and for some products, unlimited use of third-country fabrics. These provisions are permanent greatly outweigh those of the Caribbean Basin Trade Partnership Act (CBPTA), signed in 2000. The CAFTA-DR agreement offers a basis for competitiveness.

¶10. (U) Even so, the CAFTA-DR agreement has not entered into force for the Dominican Republic. Discussions continue on specific changes in laws, regulations and procedures required for the U.S. president to certify compliance; this could happen in early 2007. The tangible effects of the delay in implementation can be estimated by looking at Guatemala and El Salvador, where textile exports to the United States substantially increased following implementation. In El

Salvador alone exports to the United States increased by USD 70 million over the same period last year. The Dominican Republic has reported only decreases in its textile exports to the United States.

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OBSTACLES
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¶11. (SBU) Although the CAFTA-DR agreement could be a life-preserver for the textile/apparel sector in the Dominican Republic, the country carries with it many burdens that could still sink the sector altogether. The Dominican peso has been overvalued by up to 15 percent opn a purchasing power parity basis since October 2004, due to tight monetary policy. The electricity sector is characterized by low payment indices, a lack of financing, subsidies untenable in the medium term, near-total government control of distribution, and cross-debts of more than USD 500 million; the practical result is high electricity rates and frequently interrupted supply. Many -- perhaps most -- apparel manufacturers must generate their own electricity, much of the time, adding to costs. Another issue of concern was the decision in June of 2006 by Customs Director General Miguel Cocco to charge a "service fee" of 0.4 percent of the CIF value of all merchandise entering the Dominican Republic, including that for the FTZs. This action created an uproar from the textile/apparel manufacturing companies in the FTZs. Sarah Lee cited the tax on those terms as having a negative USD 2 million impact on their annual operations, an amount that could jeopardize its operations in the Dominican Republic and cost the country 1,600 jobs. After months of difficult negotiations, Customs signed an agreement with FTZ companies to calculate the service fee according to volumes (e.g., a flat customs fee of USD 100 per 40-ft container and a maximum of USD 60 for smaller shipments). Embassy expects that similar treatment for non-FTZ companies will be required for DR-CAFTA entry into force.

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LOOKING AHEAD
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¶12. (U) USAID recently contracted consulting firm Nathan Associates to update its analysis of apparel export performance from 2001 to 2005 and to project 2006 numbers. The results are as expected: for 2006, apparel exports to the United States are likely to fall from a little over USD 1.8 billion in 2005 to USD 1.5 billion, an almost 20 percent drop. Another projected outcome from the study is that the average unit price of U.S. imports of cotton trousers is expected to increase in the Dominican Republic, losing competitiveness vis-a-vis the world average due to high electricity costs and an increase in salaries.

¶13. (SBU) The potential effects of continuing falls in the textile market are increases in unemployment and poverty, possible increases in social unrest, and increases in illegal immigration.

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COMMENT
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¶14. (SBU) There is a future for the textile and apparel sector in the Dominican Republic. The Dominican Republic's proximity to the United States along with Caucedo Port's CSI certification are major advantages. Additionally, CAFTA-DR makes permanent many benefits under CBTPA and thereby gives the Dominican Republic a boost. But textile and apparel producers must enhance their competitiveness by focusing on diversification of exports, higher value added, and faster production and delivery. Further job losses in the textile

and apparel sector are likely, due to the overvaluataion of the peso, the unresolved problems of high costs and uncertain delivery for electricity, and the perceptions of an uncertain business environment. End Comment.
HERTELL